

I v. I Exclusion Bars Coverage for Claims Brought by State Insurance Commissioner

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A state trial court, applying Pennsylvania law, has held that the insured v. insured exclusion in a D&O policy applied to bar claims brought against insured directors and officers by the Pennsylvania insurance commissioner because the commissioner, appointed by law as the insured's liquidator, was a successor to the insured within the meaning of the exclusion. *TIG Specialty Ins. Co. v. Koken*, 2004 WL 1725707 (Pa. Commw. Ct. Aug. 3, 2004).

An insurer issued a D&O policy to a company that was a third-party administrator for medical benefits. The company later purchased another company, creating a wholly owned subsidiary with which there was an existing agreement to provide third-party administrative services. Although the D&O policy was issued only to the parent company, the policy also covered the directors and officers of the subsidiary. The policy contained an exclusion that barred coverage for "any Claim made against any Insured arising out of...[a]ny Claim brought by, on behalf of or at the behest of the Company, its successor, its assignee, its trustee in bankruptcy, its debtor-in-possession, or its litigation trustee."

After the state insurance commissioner placed the subsidiary company into liquidation and was appointed by statute as the company's liquidator, the commissioner brought suit against the directors and officers of the subsidiary alleging breach of fiduciary duty, civil conspiracy, professional negligence and statutory voidable transfers. The insurer instituted this declaratory action to determine whether the insured v. insured exclusion applied to bar coverage for the claims against the directors and officers of the subsidiary brought by the liquidator.

The trial court ruled in favor of the insurer, holding that the exclusion applied to bar coverage for the state insurance commissioner's claims, as the subsidiary's successor, against the directors and officers of the subsidiary. The court first determined that the plain meaning of the term "successor" meant "[o]ne that succeeds or follows; one who takes the place that another has left, and sustains the like part or character." Further, the court noted that "[c]ommon to all [of the] definitions [of "successor"] is the concept that, by assuming the interests of another, one takes the other's place." Based on the court's prior order allowing the liquidation of the subsidiary, the court stated that, pursuant to Pennsylvania's Insurance Act of 1921, the "Court's liquidation order in the instant case 'vested [the Liquidator] with title to all property, assets, contracts of rights of action of [the subsidiary], or whatever nature and wherever located, whether held directly or

indirectly...." The court concluded that "[t]hese provisions from the Insurance Act are consistent with the definitions set forth for the term 'successor.' The Liquidator, 'by operation of law [has] succeeded to the interest' and 'rights [and] responsibilities' of the insurer." The court therefore held that the state insurance commissioner was the subsidiary's successor for purposes of the exclusion.

The commissioner argued that the term "liquidator" was not specifically enumerated in the exclusion, therefore rendering the exclusion inapplicable or ambiguous. The court rejected this contention, stating that "[t]he inclusion of several forms of involuntary successors arising from insolvency does not necessarily mean that the policy's failure to specifically identify the Statutory Liquidator removes [the commissioner] from the exclusion...." The court also refused to adopt the commissioner's attempts at "frustrat[ing] the plain meaning of the language used."

Further, the court rejected the contention that the commissioner could not be the "successor" because, as a liquidator, the commissioner also represents the interests of the subsidiary's creditors. Disagreeing, the court noted that, in its prior decisions, it has held that "when an insurance company is placed in liquidation, the Liquidator 'steps into the shoes of the insurer,' thereby 'enforcing the rights of the company and other interested individuals.'"

The court thus determined that "because the definitions do not require that a successor must necessarily maintain the same structure as the original entity, as long as the successor succeeds to the assets and rights of the original entity, and because the statute and persuasive precedent both clearly establish by operation of law such a transfer between the insurer to be liquidated and the Liquidator, we hold that the Liquidator can function as a type of successor under the plain meaning of the term in the insurance policy exclusion." Thus, irrespective of whether the commissioner represented interests beyond those of the liquidated insured, it still operated as a successor, and the exclusion thus applied.

The individual insureds also contended that an exception to the insured v. insured exclusion applied. That exception provided: "[T]his exclusion shall not apply to...derivative suits brought or maintained on behalf of the Company by one or more persons who are not Insureds and who bring and maintain the Claim without solicitation, assistance or active participation of the Company or any Insured...."

The insureds argued that the commissioner's action was akin to a derivative suit and that the exception should therefore apply because the suit was brought without the assistance or involvement of the insureds. The court rejected this argument, noting that, because the liquidator was acting as the insured company's successor, the suit was necessarily brought with the company's assistance and participation.

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